AgriBank

June 19, 2014

Mr. Barry F. Mardock
Deputy Director
Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090

Dear Mr. Mardock:

AgriBank appreciates the opportunity to respond to the proposed Standards of Conduct regulations that were published in the *Federal Register* on February 20, 2014. These comments are intended to supplement the Systemwide comments submitted to you by the Farm Credit Council.

AgriBank strongly supports ethical behavior and a culture of integrity. We fully comply with the current Standards of Conduct (SOC) regulations and have found them to be very comprehensive, allowing us to effectively deal with inappropriate behavior in a prompt and effective manner. Every employer recognizes that there are sometimes those that choose to take some inappropriate action, fully understanding that such action is unacceptable to the employer. The current regulations allow us to evaluate such actions and impose adverse consequences commensurate with the action taken, including removal of a director or termination of an employee. In fact, the Bylaws of most institutions provide that the seat of a director found to have committed a SOC violation is automatically vacated, thus quickly resolving that issue.

The proposed regulations appear to impose far greater administrative responsibility on the SOC Official, and, to some extent, upon all directors and employees. We do not believe that these additional administrative functions will have a deterrent effect upon either directors or employees. In our experience, SOC and/or criminal violations do not occur because a director or employee does not understand that their behavior is unacceptable, but rather because the director or employee believes that such behavior will not be discovered, thus they will not be held accountable for such behavior. Imposing a more burdensome administrative process does not increase the likelihood of discovery of such actions, nor act as a deterrent to such activity. Thus we would ask that FCA further consider the administrative burden created by the regulations, particularly in regard to institutions that do not have a large employee base.

We are also concerned with what appears to be a change in focus by the FCA. The existing regulations appropriately place responsibility on directors and employees to comply with the SOC restrictions and to make full disclosure of potential conflicts on a timely basis. The SOC Official then reviews those disclosures and determines whether a conflict exists based upon the information provided in the disclosure. The proposed rule appears to place much greater responsibilities on the SOC Official to independently gather additional information, determine the accuracy of information provided, and to perhaps investigate the underlying facts. The SOC Official is not equipped to do so and should not be made responsible for determining whether others have made complete and accurate disclosure. FCA should clarify that the responsibility for disclosure and reporting, and ultimately compliance, lies with each individual director and employee and that the SOC Official's responsibilities are in regard to dealing with information disclosed by those directors and employees.

In addition to the general comments above, we have the following comments regarding individual sections of the proposed rule:

612.2130 – The proposed regulation defines "agent" as any person who represents a System institution in contacts with third parties or who provides professional services to a System institution. We have no objection to including persons who represent a System institution in dealing with third parties within the definition of agent. We object however to including mere vendors to the System within the definition of agent. A third party who sells a product or service to a System institution is a vendor to the institution, they are not an agent of that institution. A principal-agent relationship is a rather precise legal relationship that carries with it far-reaching responsibilities and potential liabilities. An agency relationship is not created unless the principal has the right or authority to control the agent's conduct in the course of the agent performing a service on behalf of the principal. That simply does not exist in a vendor-vendee relationship. We are careful in drafting vendor contracts with third party vendors to clearly state that such a vendor is not an agent of AgriBank. We do this not to avoid any sort of SOC compliance, but rather to prevent AgriBank from being held liable for any actions of that third party by those who would attempt to characterize such third party vendor as our agent. If we are in fact the principal for such agent we may well be financially liable for any damage to a third party caused by the actions of our purported agent. We fear that third parties may use this regulatory definition to attempt to convert mere vendors into agents, solely to have access to our financial resources as the principal of that agent. If FCA wishes to impose responsibilities upon us in our dealings with vendors, we would suggest that the proposed rule clearly identify that such provisions apply to vendors, rather than adopting a definition of agent that is overly broad in an attempt to include third parties who truly are nothing more than a vendor to the System entity.

612.2130 - The proposed definition of "Code of Ethics" states that such a Code is used to "ensure" the ethical conduct of those who sign it. We trust that FCA recognizes that mere execution of a Code of Ethics will not ensure the ethical conduct of those that execute it. We are concerned that any SOC violation will be construed as evidence of an inadequate Code of Ethics in that such Code failed to ensure compliance. We ask that FCA revise this definition to set out a more realistic definition of a Code of Ethics that can be met by institutions by adopting a complete and carefully thought-out Code of Ethics.

612.2135 – The proposed regulation requires that directors and employees "must observe" the "letter and intent" of all applicable local, state and Federal law and regulations. We completely agree that all directors and employees must comply with all such laws. It is not clear to us how one determines the "intent" of a law aside from its "letter". We therefor ask FCA to reconsider whether you truly expect institutions to speculate as to the "intent" of any law or regulation.

We strongly object to the requirement that directors and employees must comply with all "policy statements, instructions, procedures, and guidance of the Farm Credit Administration." "Instructions" and "guidance" are not defined anywhere in the statute or regulations and thus could include virtually any communication from FCA, including any verbal comments made in a casual setting. Such guidance would presumably include verbal discussions between examiners and System employees during the examination process, even before the examination is completed, and vary widely throughout the System. Failure to comply with such instruction or guidance could subject a director or employee to all consequences for failure to comply with an FCA regulation, including the potential for civil money penalties if the failure to comply with such "guidance" is deemed to be intentional.

Again, we do not object to the requirement that directors and employees comply with all applicable laws and regulations. However, we do ask that FCA amend the proposed rule to delete the requirement that directors and employees comply with such vague requirements as are included within "policy statements, instructions, procedures and guidance". FCA should not be uncomfortable with such an approach in that FCA has the ability to adopt, through the proper regulatory process, any requirement that FCA believes is appropriate for inclusion in a binding regulation.

612.2140 – Subsection (a)(1) of the proposed regulation requires a director to disclose the names of any immediate family members who had transactions with the director's institution at any time during the reporting year. This disclosure requirement is not limited to information that the director knows, or has reason to know, thus the regulation actually requires the director to disclose information that they do not know. We object to any director being required to disclose information that they simply do not know. While it seems quite obvious that a director is simply not capable of disclosing information that they do not know, that is in fact the requirement of the proposed regulation. We would also object to any requirement that a director must affirmatively inquire of the personal affairs of any other party, so that he then "knows" the information, and thus is then required to make a disclosure. We simply fail to follow the logic of requiring anyone to disclose information that they do not know, or have some reason to know. We likewise fail to understand what purpose this is possibly intended to serve.

We ask that FCA amend the proposed rule to limit this disclosure requirement to information that the director knows, or has reason to know. If a director does not know, or have reason to know, there can be no inappropriate behavior by that director. We recognize that determining whether a director knows, or has reason to know certain information is a subjective criteria, however we are comfortable that both the SOC Official, and FCA, is capable of making that determination.

We are also aware that a similar requirement is imposed on senior officers of System institutions in Section 612.2150 and upon both directors and senior officers in Part 620 of existing regulations. We therefore also request that FCA take this opportunity to revise those requirements to be consistent with the above.

612.2145 – Subsection (a)(7) prohibits a director from borrowing from a borrower of a System institution. Subsection (b)(4) provides an exception to that prohibition if the SOC Official determines in advance that the transaction is in the ordinary course of business or is not material in amount or value. While we appreciate FCA creating this exception, the value of this exception is greatly minimized by requiring prior approval of the SOC Official. We request that the proposed rule be amended to provide that any transaction that is in the ordinary course of business be exempt from the (a)(7) prohibition. The director would then be responsible for initially determining that such transaction is in fact in the ordinary course of business. If it is later determined that the transaction was not in the ordinary course of business, the director is not entitled to the benefit of the exception and will incur any consequences. This will allow directors to enter into purchase transactions with seller financing in the ordinary course of their business without the obligation of first determining whether the party with whom they are doing business is in fact a System borrower. If the transaction is truly in the ordinary course, there should be no conflict of interest concerns regarding that transaction.

612.2160 – The proposed rule requires that each institution "ensure" compliance with this rule by its directors, officers and agents. It simply is not possible for any institution to "ensure" that its directors, officers and agents do anything, including complying with this rule. The institution can set in place requirements, processes, procedures, etc. that require directors, officers and agents to perform such

actions, but it cannot ensure that they will comply with those requirements. The institution can clearly impose sanctions for failure to satisfy the identified requirements, including the removal of a director or termination of the employment of an employee, but that is not ensuring their compliance with this rule. The proposed rule should be amended to delete the requirement that the institution ensure compliance of others.

612.2160(f) – The proposed rule requires each institution to provide to its agents a copy of the institution's SOC policy and Code of Ethics. Section 612.2180(b) of the proposed rule requires agents to certify that they will adhere to the agent's ethics standards or to the institution's Code of Ethics provisions "applicable to agents". Given the limited nature of that certification, there is no need to provide to an agent the institution's entire SOC policy, but rather only the Code of Ethics, or perhaps only those provisions of the Code of Ethics applicable to agents. We assume that agents will object to the administrative burden imposed by the proposed rule, and that the additional burden will result in higher pricing at the expense of the System institution. That additional expense can be reduced by burdening those agents only with the institution's Code of Ethics rather than both the Code of Ethics and the entire SOC policy.

612.2165(j) – The proposed rule requires a bank's policies and procedures to outline the responsibilities of the SOC Official to review all prior approval loans for compliance with the SOC regulations. This approval is an addition to the responsibilities imposed upon the director or employee seeking that loan, and the responsibilities imposed upon the association that has originated that prior approval loan. This additional level of review serves no valid purpose and will greatly slow the prior approval process, particularly in regard to loans approved through the use of a scorecard. The borrower provides limited information for consideration when using the scored loan process. That limited information is likely inadequate to provide assurance to the bank SOC official that the borrower and the loan transaction itself are in full compliance with the applicable regulations. As part of our prior approval process we require each association to certify on every prior approval loan that all involved transactions are in full compliance with all SOC provisions. That association certification should be sufficient in that the association is in the best position to understand all of the underlying facts and circumstances, and they generally have far greater knowledge about the loan applicant. We therefore ask that FCA remove this additional level of conflict approval, which will allow the scored loan process to remain available to those applicants.

612.2180 – As stated above, we ask that FCA revise the definition of agent to include only those that are truly agents of the institution, and not include mere vendors of products or services to the institution within that definition.

We fully agree that agents of the System should maintain high standards and avoid conflicts as set out in subsection (a). We also agree that System institutions must make sound business decisions in dealing with agents as set out in subsection (b). We strongly disagree, however, that FCA has the authority to regulate such agents and to require that they provide a certification of any sort to a System institution. We also object to FCA's regulatory conclusion that we are legally responsible (liable) for all of the actions of our agents. Such liability determination can only be made by a court of law and will be based upon the facts and circumstances of each particular situation. We believe that it is an unsafe and unsound

practice for FCA, as our regulator, to publicly state that System institutions are conclusively "responsible for the actions of their agents". If this provision remains, we will simply have no legal defense to damage claims from third parties based upon the actions of our "agents". The potential for such claims, and the related liability, is all the more reason to very narrowly define the term "agent" as requested above.

We also believe that requiring such "certification" by any agent will result in an increase in costs to System institutions. Such agents will be concerned about their liability for such certification and will generally seek legal advice regarding their exposure. Imposing this additional business concern, and additional cost, upon an agent, will negatively impact their interest in dealing with System institutions, and will ultimately result in increased cost or fewer vendor options being available to the System.

We ask that FCA revise the proposed rule to only impose requirements on System institutions, not upon these non-System entities. The bulk of Section 612.2180 is well written and will serve the System well, and we do not object to those provisions. More specifically, we ask that FCA delete all but the first two sentences of subsection (b), and revise subsection (d) to prohibit a System institution from selling such property to an agent, rather than attempting to regulate the non-System agents in regard to purchasing property from a System institution.

As always, we appreciate the opportunity to provide these comments. If you have any questions regarding the above, please feel free to contact me at your convenience.

Sincerely,

William J. Thone
Vice President & General Counsel